

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

Application of SOUTHERN CALIFORNIA
EDISON COMPANY (U 338-E) to Report on the
Valuation Process for Certain Generation-Related
Assets Pursuant to D.97-11-074.

Application 98-05-014

Application of PACIFIC GAS AND ELECTRIC
COMPANY to Report Assessments of Inventory
Balances and to Address Appraisal of Retained
Generation Assets.

(U 39 E)

Application 98-05-022

**SCOPING MEMO AND RULING
OF ASSIGNED COMMISSIONER**

Pursuant to Article 2.5 of the Rules of Practice and Procedure, this ruling sets forth the procedural schedule, designates the principal hearing officer, and addresses the scope of these proceedings following prehearing conferences held on October 1, 1998, and January 13, 1999.

Procedural Summary

On October 20, 1998, Pacific Gas and Electric Company (PG&E) and Southern California Edison Company (Edison) each filed a Proposed Scoping Memo and Ruling of Assigned Commissioner.¹ Comments were filed by Enron

¹ Since San Diego Gas and Electric Company (SDG&E) does not have power plant appraisal issues, its Application (A.) 98-05-041 is addressed separately.

Corp. (Enron), and jointly by the Office of Ratepayer Advocates (ORA) and The Utility Reform Network (TURN). Also, comments and a motion for permission to file late comments was filed by the Association of California Water Agencies (ACWA). ACWA's motion to file late comments is granted. PG&E filed its proposed appraisal process on December 11, 1998.

A second prehearing conference was held on January 13, 1999. Prehearing conference statements were filed by numerous water agencies, customer representatives, environmental groups and market participants. Parties at the prehearing conference addressed issues surrounding the proper scope of the proceeding, schedule and categorization.

On January 13, 1999, ORA and TURN filed motions to dismiss without prejudice the applications of PG&E and Edison. Responses to the motions were filed January 28, 1999 by the California Department of General Services, Enron, Friends of the Eel River, California Sportfishing Protection Alliance, and Pacific Coast Federation of Fishermen's Associations, PG&E, Edison, and James Weil.

Scope of the Proceeding

Retained Generation Asset Issues

This proceeding was designed with a simple purpose, as laid out in Decision (D.) 97-11-074, to establish principles to arrive at a "market value" for assets retained by the utilities.² It was not designed to establish the market value

² In Ordering Paragraph 17 of D. 97-11-074, the Commission stated:

"In order to fully comply with Public Utilities Code § 367(b), PG&E, Edison, and SDG&E shall file applications no later than March 2, 1998 to establish the **principles** necessary to appraise their retained assets and to report assessments of the materials and supplies inventories, and, for Edison, the fuel inventories. As described in this decision, Edison shall include a proposal to ensure that ratepayers continue to benefit from the revenue-sharing mechanism for fuel oil

Footnote continued on next page

for a given asset, nor to authorize the utilities to dispose of any asset. While it is appropriate for the Commission to adopt general principles for valuation of retained assets here, Assembly Bill (AB) 1890 and Commission precedent indicate that the market valuation of specific assets that are to be sold or transferred should be performed in later asset-specific proceedings. If the decision is made to retain an asset, then pursuant to PU Code § 377, the utility must demonstrate to this Commission's satisfaction that retention of the asset is in the public interest, and does not confer undue competitive advantage, but this proceeding is not the place for this determination.

In addition, PU Code § 367(b) identifies that valuation of assets, for purposes of calculating uneconomic costs, must be completed not later than December 31, 2001 using appraisal, sale, or other divestiture. Because the code identifies the purpose of this market valuation to be determination of uneconomic costs, the market value arrived at for that purpose may not correspond to future market value at the time such assets are exposed to market risk or retired. To the extent that a utility decides to sell or transfer an asset, whether to an affiliate or third party, or otherwise expose it to market risk, at some point after it has been market valued, any such disposition is governed by PU Code § 851 and/or § 377. The Commission has the ability and the discretion under the law to conduct a PU Code § 851 review separate from this proceeding,

inventory, adopted in D.94-10-044. Edison shall also include, in this application, its pro-rata analysis of its land, according to its function, i.e., transmission-related, fuel oil pipeline-related, and generating plant-related, as well as Edison's proposal for treatment of fuel-oil pipeline land that is consistent with D.94-10-044." (D.97-11-074, emphasis added.)

and to require CEQA review. AB 1890 did not repeal PU Code § 851 or bar CEQA review.

Some parties have recommended that this proceeding must explore whether appraisals should even be allowed to determine market value. Section 367(b) clearly allows for appraisal as one means of arriving at market value. It is my personal belief that the best measure of market value is discovered through the use of market mechanisms. However, there are some circumstances where outright sale of an asset may not be appropriate, feasible, or in the public interest and for that reason, we must establish a means of valuing those assets, for purposes of calculating uneconomic costs. These principles could contain market mechanisms beyond the approaches identified by PG&E and Edison. Those parties who believe PG&E and Edison's proposed principles are deficient will have the opportunity to propose alternatives to the applicants' principles. This scoping memo does not prejudge the best means of determining market value for retained assets. In addition, the mere fact that we adopt such principles does not, and should not, imply that the utility will decide to retain an asset.

This proceeding does not prejudge whether retention or disposition of any particular asset is in the public interest. Clearly, sale or transfer of these assets presents many challenging public policy questions, among them issues of market power, the environment, water rights, agricultural impacts, local public and private socioeconomic impacts, statewide resource and infrastructure issues, issues related to the public interest and resources held in the public trust, interstate and federal issues, and issues related to the federal fiduciary responsibility for certain populations. If a transfer to an affiliated company is proposed, compliance with the Commission's affiliate transaction rules must be examined. All of these issues are appropriately addressed in the particular § 851

and § 377 proceedings that will arise out of the assessment by a utility of whether to retain or dispose of an asset.

It is also clear that if a utility decides to sell or transfer any of its remaining generation assets, the ensuing proceeding has the potential to be quite complex. The complexity of any ensuing proceedings must be balanced with the statutory requirement that market valuation be completed by December 31, 2001. Therefore, the parties should address the need for a date certain by which utilities must identify the assets they plan to retain, sell, transfer, or otherwise dispose of. If a date certain is needed, parties should propose appropriate timelines and procedural vehicles to accomplish this objective. PG&E and Edison may supplement their testimony in this respect.

Consistent with this scope, the parties should be allowed to present testimony regarding how the Commission can best determine the fair market value of the utilities' retained generation assets. In so doing, the parties may present alternatives to appraisal, as proposed by the applicants, and critique the ability of appraisals to establish fair market value for retained assets, generally or for particular plants. However, this is not the proceeding where the Commission is reviewing particular PU Code § 851 transfers and PU Code § 377 public interest and anticompetitive impacts. I encourage parties to identify what types of constraints (operational or otherwise) should be taken into consideration in arriving at market value for these assets so that we may assure continued operation in the public interest.

Any discussion of specific assets will only serve to provide the context in which to examine various market valuation methods. The actual valuation and disposition of these assets will be subject to PU Code § 851 filings and Commission approval in subsequent proceedings. Also, examination of water

rights, water quality, and water delivery issues related to individual plants should be reserved for subsequent proceedings.

Other Issues

PG&E's and Edison's applications also address how to handle materials and supplies, fuel inventories, and land for purposes of market valuation. Enron, ORA and TURN are in general agreement with some of the proposals of the utilities on these issues, but all parties appear to concur that evidentiary hearings are not needed to address these matters. These issues are within the scope of the proceeding and I agree with the parties that this portion of the case should be submitted for decision on the basis of briefs.

Need for Hearing

PG&E, Edison, and Enron believe that the issues in these proceedings may be adequately addressed through paper hearings. However, PG&E and Edison do not object to holding hearings for the limited purpose of addressing issues related to appraisal of the utilities' remaining power plant assets.

I agree that the request of ORA and TURN for evidentiary hearings should be granted. All parties may present testimony on the principles and the process of appraisal as described above.

At the first prehearing conference, ORA proposed that its expert witnesses on appraisal principles not be required to provide prepared testimony. ORA's request is denied. As is usual in Commission evidentiary hearings, all expert witnesses should provide prepared testimony prior to cross-examination.

Issues related to materials and supplies, fuel inventories, and land will be addressed separately through written pleadings.

Category of Proceeding

The Commission preliminarily categorized these proceedings as ratesetting. Enron and PG&E agree with the Commission's preliminary determination that the category of these proceedings is ratesetting.

Edison states that its proposed appraisal principles for generation assets establish a policy of general applicability to any of the investor-owned electric utilities. In contrast, Edison states that issues related to materials and supplies, fuel inventories, and land involve utility-specific facts that will determine rate recovery of certain costs. Edison, therefore, proposes that these proceedings be bifurcated, with the appraisal principles to be established via a quasi-legislative process, and the remainder of the application to be categorized as ratesetting.

Initially, ORA argued that the entire proceeding should be categorized as ratesetting. Now, ORA states that further investigation into hydro and coal market valuation has caused them to rethink their position. ORA now recommends that the Commission categorize these applications as quasi-legislative for the market valuation of the hydro and coal generating plants. ORA argues that the decision in these applications will not have a direct impact on rates; that would occur later. Further, ORA argues that categorization of these proceedings as quasi-legislative would help potential bidders for the plant, competitors of the affiliates of PG&E and Edison, local agencies and groups concerned about local land and water issues, and, of course, ratepayer groups to inform the Commission of their interests and concerns regarding market valuation.

The primary objective of these proceedings is to assist the Commission in determining the final calculation of uneconomic costs. Therefore, the applications of PG&E and Edison, at least in part, fit the definition of ratesetting. On the other hand, Edison makes a reasonable argument that the part of these

proceedings related to appraisal principles fits the definition of quasi-legislative proceedings, which Rule 5(d) defines as follows:

“‘Quasi-legislative’ proceedings are proceedings that establish policy or rules (including generic ratemaking policy or rules) affecting a class of regulated entities, including those proceedings in which the Commission investigates rates or practices for an entire regulated industry or class of entities within the industry.” (Emphasis added.)

Therefore, it appears that the applications of PG&E and Edison do not squarely fit into any one category. The Commission’s rules address this situation. Specifically, Rule 6.1 states:

“(c) When a proceeding does not clearly fit into any of the categories as defined in Rules 5(b), 5(c), and 5(d), the proceeding will be conducted under the rules applicable to the ratesetting category unless and until the Commission determines that the rules applicable to one of the other categories, or some hybrid of the rules, are best suited to the proceeding.”

Accordingly, I conclude that the applications of PG&E and Edison should be categorized as ratesetting.

Schedule

Principles of Market Valuation for Retained Assets

Given the scope of this proceeding described above, the schedule is as follows:

Other parties serve prepared testimony, applicants serve supplemental testimony on “date certain” issues	3/2/99
Rebuttal testimony	3/16/99
Evidentiary hearings	3/22-24/99

Concurrent opening briefs	4/19/99
Concurrent reply briefs	5/3/99
ALJ's proposed decision	6/3/99

My goal is for the Commission to issue a decision in this matter at the July 8, 1999 Commission meeting, but in no event will resolution exceed 18 months from the dates of filing of the applications. Some parties have requested that the Energy Division hold workshops on various issues, among them Federal Energy Regulatory Commission (FERC) relicensing and tax issues associated with divestiture. As the purpose of this proceeding is limited to valuation of retained assets, rather than divested assets, I will not order such workshops at this time. However, parties should renew their request for workshops if they believe that such workshops would be helpful in developing principles for valuing retained assets.

Other Issues

Concurrent opening briefs on the materials and supplies, fuel inventories, and land issues should be filed no later than March 2, 1999. Concurrent reply briefs should be filed no later than March 16, 1999. My goal is for these issues to be decided in May 1999, but in no event will resolution exceed 18 months from the dates of filing of the applications.

Consolidation

I conclude that the issues related to market valuation principles for retained assets should be consolidated for hearing and decision. The issues related to materials and supplies, fuel inventories, and land will not require hearings and may be handled separately for each utility.

Assignment of Principal Hearing Officer

Rule 6(a)(3) requires that this ruling designate a principal hearing officer. The assigned Administrative Law Judge will be the principal hearing officer in these proceedings.

Motion to Dismiss

On January 13, 1999, ORA and TURN filed a motion to dismiss without prejudice PG&E's application. On the same day, they filed a similar motion regarding Edison's application. ORA and TURN raise four main points in the motions:

1. The applications violate the Commission's affiliate transaction rules;
2. The testimony is incomplete by failing to identify the assets at issue;
3. Failure to provide adequate notice through failure to serve affected interests; and
4. Inconsistency between PG&E's initial and amended applications.

A wide range of arguments was presented in responses to the ORA/TURN motion. I believe that the scope of this proceeding, as described above, adequately addresses the concerns raised by ORA, TURN and others regarding point 1 by identifying that PU Code §§ 851 and 377, and the Commission's affiliate rules would apply to any disposition of assets.

PG&E and Edison argue that to the extent the Commission's affiliate rules are in conflict with AB 1890, the affiliate rules must yield to the statute. Since the applicability of the Commission's affiliate rules to utility assets is beyond the scope of this proceeding, and will be addressed in necessary subsequent proceedings, PG&E and Edison's argument is not ripe for adjudication, but may properly be raised in the later asset-specific proceedings.

In response to ORA and TURN's request that the Commission direct PG&E "to prepare to auction" hydroelectric assets, PG&E additionally argues that the

Commission can neither order the “forced sale,” nor “compel retention” of PG&E’s hydroelectric facilities.³ PG&E’s concern is both misplaced and beyond the scope of this proceeding. The Commission has not proposed any forced asset sale or compelled asset retention. However, as described above, and consistent with the requirements of AB 1890, the Commission will review PG&E’s (and Edison’s) proposed disposition or retention of generation assets and their market valuation in subsequent proceedings.

With respect to Point 2, I also believe that the scope as I have described it responds to this concern.

Points 3 and 4 are interrelated. Point 4 is essentially an additional argument with respect to insufficient notice through failure to adequately describe the requested relief. Point 4 applies only to PG&E’s application. The points regarding notice do have merit, however, I believe that this deficiency of service can be corrected in a less extreme manner than dismissal. Accordingly, PG&E and Edison are directed to serve their applications, including amendments, and this scoping memo on local jurisdictions, such as cities, counties, special use districts, and federal and state resource agencies, where generation assets are located within ten days of the date of this ruling. The applicants should include a letter that identifies generation assets in that jurisdiction may be subject to the principles for market valuation of retained assets that will be developed in this proceeding. The letter should include contact information for the Commission’s Public Advisor (in both San Francisco and Los Angeles) in the event local jurisdictions are interested in participating in

³ Edison makes a similar argument regarding Commission-required retention of a generation asset.

the proceeding. The applicants shall provide a draft of the letter to the Public Advisor within five days of this ruling. The Public Advisor shall review and approve the notice prior to its mailing.

The motions of ORA and TURN to dismiss the applications without prejudice are denied.

Request for Order Instituting Investigation or Rulemaking

On December 11, 1998, ACWA filed a request that the Commission open an investigation into the future ownership and control of utility hydroelectric assets. As described within the scoping portion of this ruling, parties in this case have identified many complex issues with respect to disposition of generation assets. As described above, this proceeding is limited to valuation issues for retained assets, therefore, it is appropriate for us to consider whether a more comprehensive proceeding regarding disposition of assets is necessary at this time. I will treat ACWA's request as a motion for purposes of filing with the Docket Office.

I have concluded that it would be premature at this time to open an investigation or rulemaking into these issues, given the uncertainty surrounding disposition of the hydroelectric assets. When there is a clearer picture regarding whether the utilities will dispose of their hydroelectric assets, ACWA should renew its request, if appropriate, for a comprehensive proceeding regarding disposition of assets. The Commission may also consider such an investigation or rulemaking on its own motion at that time. The motion by ACWA for a comprehensive proceeding regarding disposition of assets is denied without prejudice.

Exchange of Documents by E-Mail

In some proceedings, parties, staff and Commission decision makers have found it useful and efficient to use electronic transmission to convey testimony,

pleadings, Commission documents and less formal communications. The use of electronic transmissions may be especially helpful where review times are short. Parties who wish to be included as recipients of an electronic service list and electronic transmissions in this proceeding should forward their e-mail addresses to BDP@cpuc.ca.gov no later than February 12, 1999. The ALJ will electronically transmit a list of those addresses shortly thereafter to those who have submitted them.

IT IS RULED that:

1. The purpose of these proceedings is to establish the principles necessary to market value the utilities' retained generation and generation-related assets for purposes of calculating uneconomic costs.
2. These proceedings are not the forum for market valuation of specific generation assets, and Pacific Gas and Electric Company's (PG&E) proposal for such valuations is beyond the scope of these proceedings.
3. The parties may present alternatives to appraisal, as proposed by the applicants, and critique the ability of appraisals to establish fair market value for retained generation assets.
4. If PG&E and Southern California Edison Company (Edison) propose to transfer to an affiliate or sell to a third party any generation assets, they shall file Public Utilities (PU) Code § 851 applications.
5. In such PU Code § 851 filings, PG&E and Edison shall address PU Code § 377 requirements concerning the public interest and anticompetitive impacts and compliance with affiliate transaction rules as they relate to the specific assets at issue.
6. Also, in such PU Code § 851 filings, PG&E and Edison shall address the requirements of the California Environmental Quality Act (CEQA) related to the specific assets at issue.

7. The request of the Office of Ratepayer Advocates and The Utility Reform Network for evidentiary hearings to present outside consultants with experience in power plant appraisals, auctions, and valuation of California water rights is granted. Likewise, at the evidentiary hearing scheduled, all parties may present their witnesses on these issues. All expert witnesses shall provide prepared testimony.

8. Issues related to water rights, water quality, and water delivery issues related to individual hydroelectric plants shall be addressed in separate PU Code § 851 proceedings for such power plants.

9. The schedule is as set forth above.

10. These proceedings shall be bifurcated as follows: (1) market valuation principles for remaining generation assets, and (2) materials and supplies, fuel inventories, and land.

11. The market valuation principles portion of PG&E's and Edison's applications shall be consolidated for hearing and decision. The materials and supplies, fuel inventories, and land portion may be handled separately for each utility.

12. These proceedings shall be categorized as ratesetting.

13. Concurrent opening briefs on materials and supplies, and land issues shall be filed no later than March 2, 1999 and concurrent reply briefs shall be filed no later than March 16, 1999.

14. The assigned Administrative Law Judge shall be the principal hearing officer in these proceedings.

15. ACWA's motion to file late comments is granted.

16. The motions of ORA and TURN to dismiss the applications without prejudice are denied.

17. The motion by ACWA for a comprehensive proceeding regarding disposition of assets is denied without prejudice.

Dated February 1, 1999, at San Francisco, California.

Henry M. Duque
Assigned Commissioner